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Attorney for the Commission Staff

## BEFORE THE IDAHO PUBLIC UTILITIES COMMISSION

IN THE MATTER OF IDAHO POWER	)	
COMPANY'S APPLICATION TO APPROVE	)	CASE NO. IPC-E-15-26
THE TRANSFER AND SALE OF CERTAIN	)	
ASSETS TO THE UNITED STATES	)	COMMENTS OF THE
DEPARTMENT OF JUSTICE, FEDERAL	)	COMMISSION STAFF
<u>BUREAU OF INVESTIGATION.</u>	)	

The Staff of the Idaho Public Utilities Commission, by and through its attorney of record, Daphne Huang, Deputy Attorney General, submits the following comments in this case.

### BACKGROUND

Idaho Power ("Idaho Power" or "Company") provides electric service to a United States Department of Justice Federal Bureau of Investigation (FBI) facility in the Company's service territory pursuant to Idaho Power's Tariff Schedule 19 (Large Power Service). Idaho Power owns and operates transformers and other facilities (hereafter, "Assets") on the FBI's side of the Point of Delivery (POD), to meet the FBI's electric service requirement under Idaho Power's Rule M addressing Facilities Charge Service. The FBI pays a monthly facilities charge to Idaho Power for this service.

On November 25, 2015, Idaho Power filed an Application with the Commission for an Order approving the transfer and sale of the Assets to the FBI. At the FBI's request, Idaho Power

entered into an Asset Sale Agreement to transfer and convey the Assets to the FBI for a purchase price of \$79,373<sup>1</sup>. Under this Agreement, the FBI agrees to obtain title to the Assets, and assume ownership, operation, maintenance, and all liabilities associated with them. The FBI will own all facilities installed beyond the POD upon sale and transfer of the Assets. The Agreement is contingent upon the Commission's approval.

## STAFF ANALYSIS

The Commission has authority to approve or reject the proposed Agreement under *Idaho Code* § 61-328. Also, all sales of facilities must be approved by the Commission under Section 3 of Idaho Power's Rule M, the tariff that governs the sale of Company-owned facilities beyond the POD. Section 3 of Idaho Power's Rule M requires:

1. Compliance with *Idaho Code* § 61-328;
2. No mixed ownership of facilities. A customer purchasing Company-owned facilities installed beyond the POD must purchase all facilities listed on the Distribution Facilities Investment Report for that location;
3. The customer must provide the operation and maintenance of all facilities installed beyond the POD after the sale is complete; and
4. The customer must prepay engineering costs for sales determinations taking more than 16 estimated hours of preparation. Sales determinations equal to or less than 16 estimated hours of preparation will be billed to the customer as part of the sales agreement, or after engineering work is completed in instances where the sale is not finalized.

Under *Idaho Code* § 61-328, the sale of Assets must meet the following criteria:

1. The proposed transaction must be consistent with the public interest;
2. The cost and rates for supplying service must not be increased because of the transaction; and
3. The FBI must have the bona fide intent and financial ability to operate and maintain the Assets in the public service.

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<sup>1</sup> Idaho Power claims portions of the Agreement are confidential and submitted a redacted copy of the Agreement as an attachment to its Application. See Rule 67, IDAPA 31.01.01.067.

In examining Idaho Power's proposed transaction with the FBI, Staff notes that its assessment here is specific to this case. Analyses of such transactions under Idaho Power's Rule M and *Idaho Code* § 61-328 depend on their unique circumstances. Staff's comments are not intended as a generic endorsement of Idaho Power's transfer and sale agreements or the methodologies used therein.

As to Rule M, the Company maintains there will be no mixed ownership of facilities, that the Agreement requires the FBI to provide operation and maintenance of all facilities beyond the POD after the sale is complete, and that the FBI will prepay engineering costs as required in accordance with Rule M. Staff accepts the Company's assurances.

The Company also asserts the transaction satisfies the requirements of *Idaho Code* § 61-328. Idaho Power states that, because the Assets only serve the FBI, the Asset sale will not affect the deliverability and reliability of electric service to other customers and is thus consistent with the public interest. Under the Agreement, the Company will install a system protection package prior to the FBI's POD. The costs of this system protection package are not included in the Asset purchase price of \$79,373, but are separately billed to, and paid by, the FBI. *See* Agreement at 3. According to the Company, the Assets are all located beyond the FBI's POD and their sole purpose is meeting the FBI's service requirements. Staff agrees that the Asset sale will not affect the delivery and reliability of electric service to other customers.

Also, the Company notes that the FBI has agreed it has the bona fide intent and financial ability to operate and maintain the Assets backed by the United States government. Staff believes that this acknowledgement satisfies the statutory requirement regarding the FBI's intent and ability to operate and maintain the Assets. The remaining requirement under *Idaho Code* § 61-328 is that the transaction must not increase the cost and rates for supplying service.

#### **Analysis of Sales Price Methodology**

Idaho Power states that its sales price methodology in this case ensures that the transaction will not negatively impact the Company or its other customers. In its Application, the Company describes its five-component methodology for establishing the sale price for the Assets. These components and the amounts associated with each are listed below:

Net Book Value	\$20,681
True-up of Past Levelized Rate of Return	\$11,955
Near Term Rate of Return Impact Resulting from Sale of Assets	\$7,428
Near Term Operational Impact Resulting from Sales of Assets	\$14,776
Net Tax Gross-up	\$24,053
Subtotal	\$78,893
Work Order Closing Costs	\$480
Total	\$79,373

The Company's treatment of each of these components relies on an approach used to compute the Rule M monthly Facilities Charge Rate, which was established as part of the Company's last general rate case and approved in Commission Order Nos. 32426 and 32481. This approach allows the Company to recover its authorized rate of return, book depreciation, operation and maintenance expenses, administrative and general expenses, income taxes, property taxes, regulatory fees, working capital, and insurance by means of a flat monthly Facilities Charge equal to 1.41% of the original costs of Company-owned equipment installed. The approach established a fixed, 31-year depreciation life for all Schedule 19 assets subject to the monthly Facilities Charge. After 31 years, the monthly Facilities Charge rate decreases to 0.59% because the Company is not authorized to recover either depreciation or a rate of return on fully depreciated capital assets.

#### Net Book Value

The Assets include facilities installed between 1974 and 2005. The Company has determined the net book value for each of these assets as original investment cost less accumulated 31-year straight line depreciation. Staff agrees with the Company's method for computing net book value, and believes its inclusion in the sales price to be appropriate.

#### True-up of Past Levelized Rate of Return

Depreciation causes the net book value of assets, the authorized return on those assets, and associated income taxes to decrease continuously over 31 years. In order to avoid the need for imposing an annually decreasing Facilities Charge, the 1.41% Rule M flat rate charge is computed to include a "levelized," time-value equivalent for these revenue requirement components. This allows a single FBI facilities charge over the life of the equipment even though net book value

decreases over time. Under the resulting levelized payment schedule, facilities charge customers effectively underpay the Company for the first 10 years of an asset's life, but then overpay for the remaining period, so the Company fully recovers its revenue requirement over the asset's depreciable life. Thus, a customer who purchases a facility from the Company before it is fully depreciated still owes the Company a "true-up" for the difference between the Company's authorized rate of return and the levelized rate recovered in the monthly Facilities Charge. Staff believes that the true-up and the Company's methodology for computing this component are appropriate.

#### Near-term Rate of Return Impact Resulting from the Sale of Assets

Idaho Power states that when a customer buys an asset subject to the Facilities Charge, the return that the Company would have earned through the Facilities Charge is foregone, that the Company has limited opportunity to re-invest those funds in other assets, and that the Company will not be able to earn its authorized rate of return until an alternate investment is recognized in a future rate case. To offset this loss, the Company has included the present value of three years of the levelized rate of return component of the Rule M Facilities Charge. The Company chose three years based on its estimate of average intervals between general rate cases.

Staff agrees that the Asset sale could result in lost return until an alternate investment is made and recognized in a future general rate case. Staff believes that this revenue loss could be a disincentive for the Company to sell its facilities to the FBI and other similarly situated customers. Consequently, Staff maintains that it is reasonable to include a revenue loss component in the asset evaluation methodology. Staff believes that inclusion of the near-term rate of return impact in the Asset sales price does not violate the requirements of *Idaho Code* § 61-328.

#### Near-term Operational Impact Resulting from Sale of Assets

A portion of the monthly Facilities Charge paid by the FBI is intended to recover costs associated with Operations & Maintenance ("O&M") and Administrative & General ("A&G") expenses. After the sale, the Company will no longer receive this revenue.

Idaho Power's pricing methodology includes three years of monthly Facilities Charge components related to O&M and A&G in order to offset the foregone revenue associated with costs related to regulatory fees, O&M, A&G, and working capital incurred on behalf of the facilities being purchased by the FBI. The Company explains that during a general rate case, the



revenue requirement for the Schedule 19 customer class includes a revenue credit, or reduction, equal to the amount of facilities charge revenue to be collected from Schedule 19 customers. Because the Company will not have an opportunity to recalculate the revenue requirement and reset rates until the next general rate case, it believes there will be a near-term operational impact resulting from the sale.

Staff believes that once the facilities are sold, Idaho Power will no longer be responsible for any associated O&M or A&G expenses or working capital. Once the O&M and A&G expenses go away after the sale, Idaho Power should, in turn, no longer need to receive a component of Facilities Charge revenue to cover these expenses. Because the expenses and the revenues are presumably equal amounts and both go away at the same time, other Schedule 19 customers should not be adversely impacted. Consequently, Staff would not include this cost component in the sales price due to any near-term operational impact resulting from the sale. Nonetheless, Staff recognizes that the FBI has agreed to the sale price and thus inclusion of the component, and that its inclusion does not appear to otherwise violate the requirements of *Idaho Code* § 61-328. Given the FBI's agreement upon its arms-length bargaining with Idaho Power, and for purposes of this particular case, Staff finds that inclusion of this component does not warrant disapproval of the transaction.

#### Net Tax Gross-up

There is a mismatch between the straight-line depreciation methodology used to determine book value and the accelerated depreciation methods used for assessing income taxes. This mismatch will generally result in some, or all, of the asset's book value being treated as a gain for income tax purposes. Accordingly, it is necessary to "gross-up" this portion of the book value, as well as any other gain resulting from the sale. Staff agrees that the Company's net tax gross-up methodology is appropriate, but believes that the computation of the gross-up amount should be based only on the components included in the Assets' sales price.

#### Summary

Staff agrees that the Company's treatment of net book value, true-up of the levelized rate of return, loss of near-term return, and net tax gross-up (based on an adjusted sales price) are appropriate and protect ratepayers as required by *Idaho Code* § 61-328. Staff disagrees with the Company about inclusion of the near term operational impacts associated with O&M and A&G in

the Assets' sales price. Nonetheless, Staff acknowledges that both Idaho Power and the FBI have signed the Asset Sales Agreement, agreeing to the sales price of \$79,373 among other terms and conditions. Despite the fact that Staff's recommendation would result in a lower sales price for the Assets, the sales price mutually agreed to by the parties will not harm other ratepayers or cause rates to increase. Thus, Staff concludes the proposed transaction satisfies the requirements of *Idaho Code* § 61-328 and is consistent with the requirements of Idaho Power's Rule M.

### **Accounting Treatment**


The Company's Application outlines the accounting treatment it will apply to the transaction if approved by the Commission. The Company's proposed accounting treatment will remove the assets from the Company's books, record the gain on the sale of the assets, and record the impact on the Company's income taxes. Staff has reviewed the proposed accounting treatment and believes it is acceptable.

### **RECOMMENDATIONS**

Upon review of the Company's Application and following the Staff's investigation, Staff recommends that the Commission approve Idaho Power Company's Application to sell assets to the FBI as proposed. Staff believes that the proposed sale meets all of the requirements of *Idaho Code* § 61-328, as well as meeting the requirements of Idaho Power's Rule M.

Should the Commission decide to approve the Application, Staff further recommends that the Commission not endorse the Company's pricing methodology as precedent going forward. Although the methodology may be appropriate for establishing asset sales prices in many circumstances, Staff believes each proposed sale is unique. Different circumstances may warrant different pricing methods or contract terms.

Respectfully submitted this 26<sup>th</sup> day of January 2016.

For:   
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Deputy Attorney General

Technical Staff: Mike Morrison  
Rick Keller  
Mark Rogers  
Donn English

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## CERTIFICATE OF SERVICE

I HEREBY CERTIFY THAT I HAVE THIS 26<sup>th</sup> DAY OF JANUARY 2016, SERVED THE FOREGOING **COMMENTS OF THE COMMISSION STAFF** IN CASE NO. IPC-E-15-26, BY MAILING A COPY THEREOF, POSTAGE PREPAID, TO THE FOLLOWING:

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